

CALIFORNIA DEPARTMENT OF MANAGED HEALTH CARE

Audit Report

SAM 20000 AUDIT

January 1, 2006, through December 31, 2007



JOHN CHIANG
California State Controller

April 2008



JOHN CHIANG
California State Controller

April 18, 2008

Lucinda A. Ehnes, Director
California Department of Managed Health Care
980 Ninth Street, Suite 500
Sacramento, CA 95814

Dear Ms. Ehnes:

The State Controller's Office audited the California Department of Managed Health Care as part of our process of studying and evaluating the accounting and administrative controls for the biennial period ended December 31, 2007. The purpose of our audit was to determine and identify any accounting and administrative control strengths and weaknesses over the department's transaction cycles.

Our audit did not disclose any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls of the California Department of Managed Health Care. However, our audit disclosed the following issues:

- Budget—Inadequate documentation of policies and procedures;
- Cash Disbursements—Reconciliations of bank accounts were not performed in a timely manner;
- Information Technology—Lack of information integrity and security and inadequate password protection; and
- Fixed Assets—Recording of fixed assets into the Inventory Database System was incomplete and not performed in a timely manner.

If you have any questions, please contact Andrew Finlayson, Chief, State Agency Audits Bureau, at (916) 324-6310.

Sincerely,

A handwritten signature in black ink, reading "Jeffrey V. Brownfield", is positioned above the printed name and title.

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/sk

cc: Ed Heidig, Chief Deputy Director
California Department of Managed Health Care
Debbie McKinney, Assistant Deputy Director
Office of Administrative Services
California Department of Managed Health Care

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Audit Report

Summary

The State Controller's Office (SCO) is in the process of studying and evaluating the internal accounting and administrative controls of the California Department of Managed Health Care in accordance with State Administrative Manual section 20060 (Internal Control Reporting) for the biennial period ended December 31, 2007. The SCO has concluded the audit.

The purpose of our audit was to determine and identify any accounting and administrative control strengths and weaknesses of the California Department of Managed Health Care.

Our audit did not disclose any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls. However, our audit disclosed the following issues:

- Budget—Inadequate documentation of policies and procedures;
- Cash Disbursements—Reconciliations of bank accounts were not performed in a timely manner;
- Information Technology—Lack of information integrity and security and inadequate password protection; and
- Fixed Assets—Recording of fixed assets into the Inventory Database System was incomplete and not performed in a timely manner.

Background

The primary responsibility of the California Department of Managed Health Care is to help California consumers resolve problems with their Health Maintenance Organizations (HMOs)—also known as health plans—and to ensure a better, more solvent and managed health care system. The department licenses and regulates California HMOs through the authority of the Knox-Keene Health Services Plan Act (Knox-Keene) and provides HMO oversight through financial examinations and medical surveys. In addition, the department develops legislation to address emerging consumer and industry issues.

Authority

State Administrative Manual section 20060 (Internal Control Reporting) states:

Pursuant to the FISMA [Financial Integrity and State Manager's Accountability Act of 1983], the head of each state entity shall prepare and submit a report on the adequacy of their entity's internal control on December 31 of each odd numbered fiscal year. . . . The report shall consist of a certification letter, the most recent audit report on internal accounting and administrative controls, and management's response to the audit report.

The California Department of Managed Health Care delegated to the SCO the duty of performing the biennial audit of internal controls in Interagency Agreement No. 07MC-1A0008, dated October 1, 2007.

Objectives, Scope, and Methodology

We studied and evaluated the accounting and administrative controls of the Department of Managed Health Care in effect as of January 7, 2008. We conducted our study and evaluation in accordance with the *Standards for the Professional Practice of Internal Auditing*, issued by the Institute of Internal Auditors, and included testing that we considered necessary to determine whether accounting and administrative controls are in place and operative.

The department's management is responsible for establishing and maintaining adequate internal controls. This responsibility, in accordance with Government Code sections 13402 et seq., includes documenting internal control, communicating requirements to employees, and ensuring that internal control is functioning as prescribed. To fulfill its responsibility, department management must assess the expected benefits and related costs of control procedures.

The objectives of our audit were to determine whether the department's internal accounting and administrative controls are in place to ensure:

- Reliability and integrity of information;
- Compliance with policies, plans, procedures, laws, and regulations;
- Safeguarding of assets;
- Economical and effective use of resources; and
- Accomplishment of established objectives and goals for operations.

The audit procedures performed included, but were not limited to:

- Reviewing the California Code of Regulations, governing statutes, the Final Budget Act, the State Administrative Manual, and any other applicable rules and regulations;
- Reviewing work performed by any external audit organization, by the department's internal audits office, or by any other departmental unit;
- Interviewing individuals involved in the various department business transaction cycles listed below;
- Documenting, analyzing, and evaluating internal controls; and
- Performing tests of procedural compliance and tests of payments, as deemed necessary.

Conclusion

Our study and evaluation did not reveal any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls of the California Department of Managed Health Care. However, our audit disclosed the following issues:

- Budget—Inadequate documentation of policies and procedures;
- Cash Disbursements—Reconciliations of bank accounts were not performed in a timely manner;
- Information Technology—Lack of information integrity and security and inadequate password protection; and
- Fixed Assets—Recording of fixed assets into the Inventory Database System was incomplete and not performed in a timely manner.

The Findings and Recommendations section of this report provides a detailed explanation of the audit findings.

In our opinion, the Department of Managed Health Care's accounting and administrative controls in effect as of January 7, 2008, taken as a whole, were sufficient to meet the objectives stated above.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all of these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

Views of Responsible Officials

We issued a draft report on January 31, 2008. Lucinda Ehnes, Director, responded by letter agreeing with the audit findings. The letter, dated February 22, 2008, is attached.

Restricted Use

This report is intended for the information and use of the California Department of Managed Health Care, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.



JEFFREY V. BROWNFIELD
Chief, Division of Audits

April 18, 2008

Findings and Recommendations

**FINDING 1—
Inadequate
documentation of
budget policies and
procedures**

The department does not have documented budget policies and procedures. It is in the department's best interest to document each job and the process of the budget cycle, in the event an employee leaves state service. It is also a best practice to document for new employees the processes that they will be performing for a better understanding of the controls that are in place.

State Administrative Manual (SAM) section 20050 (Internal Control) states:

A satisfactory system of internal control shall include an established system of practices to be followed in performance of duties and functions in each of the state agencies.

Recommendation

The department's budget unit should document each person's duties and the different steps involved in completing the budget cycle.

Department's Response

We have implemented actions to resolve each finding.

SCO's Comment

The Department has agreed to resolve this finding.

**FINDING 2—
Reconciliation of bank
accounts not performed
in a timely manner**

Bank reconciliations are not consistently performed or reviewed within 30 days of month-end. We reviewed 100% (21) of the bank reconciliations for the 21-month period from January 2006 through September 2007.

- One bank reconciliation included in the testing was not completed within 30 days of month-end.
- Four bank reconciliations were not reviewed within 30 days of month-end.

Bank reconciliations were not dated as required by SAM section 7908.

- Four bank reconciliations tested were not dated as required.

The department is not in compliance with SAM section 7901. By not performing and reviewing the bank reconciliations promptly, the department is unable to detect errors and fraud in a timely manner.

The department is also not in compliance with SAM section 7908. By not showing the date prepared on the bank reconciliations, the department is unable to determine whether the bank reconciliation was prepared in a timely manner.

SAM section 8060 (Reconciliation) states:

All bank and centralized State Treasury system accounts will be reconciled promptly at the end of each month. See SAM Section 7900 and 7967.

SAM section 7901 (Reconciliations-General) states:

All reconciliations will be prepared monthly within 30 days of preceding month. . . .

SAM section 7908 (Signatures Required on Reconciliation) states:

All reconciliations will show the preparer's name, reviewer's name, date prepared, and date reviewed.

Recommendation

The department should perform and review bank reconciliations each month within 30 days of the preceding month's end in order to detect any errors in a timely manner. Also, the department's preparer should date the bank reconciliations to determine whether the bank reconciliations were performed in a timely manner.

Department's Response

We have implemented actions to resolve each finding.

SCO's Comment

The Department has agreed to resolve this finding.

**FINDING 3—
Lack of information
integrity and security**

The department does not document requests for new-employee access to the Help Center. Supervisors request access through a telephone conversation with the Clarify IT staff. In addition, when a staff member separates from the Help Center, information is not sent to the Clarify administrators so that they can remove the user from the Clarify system.

SAM section 4841.2 (Information Integrity and Security) states:

Each agency must provide for the integrity and security of its information assets by ensuring that responsibility for each automated file or data base is defined with respect to the designated owner of the information within the agency, custodians of information and users of the information.

Recommendation

The department's Help Center should continue to develop a security request form and distribute it as soon as possible. Moreover, the Help Center should establish a policy by which it notifies Clarify administrators to delete the separating staff member's user ID from the system, and develop a reconciliation process by which supervisors can review active users and determine if those staff members are still associated with the Help Center.

Department's Response

We have implemented actions to resolve each finding.

SCO's Comment

The Department has agreed to resolve this finding.

**FINDING 4—
Inadequate password
protection**

The department does not have password protection on the Consumer Complaint Clarify system. Lack of password protection puts consumers' confidential information at risk of observation by unauthorized users of the Clarify system.

SAM section 4841.5 (Responsibilities of Owners of Information) states:

The responsibilities of an agency unit that is the designated owner of an automated file or database consist of defining precautions for controlling access to and preserving the security and integrity of files and data bases that have been classified as requiring such precautions.

Recommendation

The department should implement a computer prompt that forces Help Center staff members to enter a password to gain access to the Consumer Complaint Clarify system. In addition, the department should implement a control wherein the system will automatically shut down if it is not used for a specified amount of time.

SCO's Comment

The California Department of Managed Health Care agrees with this finding.

**FINDING 5—
Incomplete and not
timely recording of
fixed assets into the
inventory database
system**

The department does not have procedures in place to properly record recently acquired assets into the Intellitrack system. We tested 15 recently acquired assets and concluded that five assets did not have acquisition dates and two items were not entered into Intellitrack. Not recording fixed assets into the inventory system once the assets are acquired will result in inaccurate accounting of State property. If the department does not enter an acquisition date into the system, it will be unable to identify assets recorded on the property ledger or to evaluate assets for possible disposition periodically.

SAM section 8600 (Purpose and Objective of Property Accounting) states:

Property accounting procedures are designed to maintain uniform accountability for State property. These standard procedures are used to provide accurate records for the acquisition, maintenance, control, and disposition of property. . . .

SAM section 8650 (Accounting and Control of Property) states:

Departments will record the following information when property is acquired: Date acquired, property description, property identification number. . . . Departments will keep track of state property, whether capitalized or not, in an automated property accounting system (if one is used). . . .

Recommendation

The department should assign one person to update property ledgers with acquisition dates for assets over \$5,000 and record an acquisition date for each new entry to the property ledger once the asset is acquired. Reconciliation with the ledger can be simplified by using the date (fiscal month) on which the asset was recorded on the general ledger. However, any reasonable estimate of the acquisition date is preferable to a blank date field.

Department's Response

We have implemented actions to resolve each finding.

SCO's Comment

The Department has agreed to resolve this finding.

**Attachment—
Department's Response
to Draft Audit Report**



STATE OF CALIFORNIA
DEPARTMENT OF MANAGED HEALTH CARE

February 22, 2008

Andrew Finlayson
Chief, State Agency Audits Bureau
State Controller's Office
Division of Audits
P.O. Box 942850
Sacramento, CA 94250-5874

Dear Mr. Finlayson:

Subject: Response to January 2008, Department of Managed Health Care Draft Audit Report

This letter is in response to the draft report on the Financial Integrity and State Managers Accountability audit for the Department of Managed Health Care (DMHC) completed on January 7, 2008. The thoroughness of your review, and the relatively minor findings identified was a testimonial to the priority we have placed on maintaining proper internal controls.

The Department's response to the five audit findings are on the attached document. We have implemented actions to resolve each finding.

Please contact Naomi Yoshihara, Accounting Administrator, at (916) 324-5195, if you have any questions.

Sincerely,

Lucinda A. Ehnes, Director
Department of Managed Health Care

Attachment

cc: Debbie McKinney, Assistant Deputy Director, Office of Administrative Services
Naomi Yoshihara, Accounting Administrator

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Department of Managed Health Care
SAM 20000 Audit
Audit Services Performed by the State Controller's Office
January 2008

Findings

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| <p><u>Finding 1</u> Inadequate documentation of budget policies and procedures</p> | <p>SCO Reports: The department does not have documented budget policies and procedures. It is in the department's best interest to document each job and the process of the budget cycle, in the event an employee leaves state service. It is also a best practice to document for new employees the processes that they will be performing for a better understanding of the controls that are in place.</p> <p>SCO Recommendation: The department's budget unit should document each person's duties and the different steps involved in completing the budget cycle.</p> <p>DMHC Response: The Budget Office is in the process of documenting the budget policies and procedures. This will be completed by September 30, 2008.</p> |
| <p><u>Finding 2</u> Reconciliation of bank accounts not performed in a timely manner</p> | <p>SCO Reports: Bank reconciliation's are not consistently performed or reviewed within 30 days of month-end. We reviewed 100% (21) of the bank reconciliations for the 21-month period from January 2006 through September 2007.</p> <ul style="list-style-type: none"> • One bank reconciliation included in the testing was not completed within 30 days of month-end. • Four bank reconciliations were not reviewed within 30 days of month-end. • Four bank reconciliations tested were not dated as required by SAM section 7908 <p>SCO Recommendation: The department should perform and review bank reconciliations each month within 30 days of the preceding month's end in order to detect in a timely manner any errors. Also, the department's preparer should date the bank reconciliations to determine whether the bank reconciliations were performed in a timely manner.</p> <p>DMHC Response: Procedures consistent with SAM Section 7901 and 7908 were already in place. Since the audit, all accounting staff has been re-trained to perform proper bank reconciliation's in a timely manner. The Accounting Administrator will review all the bank reconciliations as a second reviewer to ensure proper procedures and timeframes are followed.</p> |
| <p><u>Finding 3</u> Lack of information integrity and security</p> | <p>SCO Reports: The department does not document request for new-employee access to the Help Center. Supervisors request access through a telephone conversation with the Clarify IT staff. In addition, when a staff member separates from the Help Center, information is not sent to the Clarify administrators so that they can remove the user from the Clarify System.</p> <p>SCO Recommendation: The department's Help Center should continue to develop a security request form and distribute it as soon as possible. Moreover, the Help Center should establish a policy by which it notifies Clarify administrators to delete</p> |

| | |
|--|---|
| | <p>the separating staff member's user id from the system, and a reconciliation process by which supervisors can review active users and determine if those staff members are still associated with the Help Center.</p> <p>DMHC Response: Help Center management has circulated new "Clarify Access Procedures," among their staff. The supervisors will use the established online service request system in order to add or delete employee access. Utilizing this system will document access requests. The Help Center has also submitted a change order request to the Office of Technology and Innovation to add the Clarify system administrator to the established online Employee Separation notice system in order to provide another deletion opportunity to ensure access deletion occurs in a timely manner.</p> |
| <p><u>Finding 4</u> Inadequate password protection</p> | <p>SCO Reports: The department does not have password protection on the Consumer Complaint Clarify system. Lack of password protection puts consumer's confidential information at risk of being observed by unauthorized users of the Clarify system.</p> <p>SCO Recommendation: The department should implement a prompt that forces Help Center staff members to enter a password to gain access to the Consumer Complaint Clarify system. In addition, a time limit should be created, where the system will automatically shut down if it is unused for a specified amount of time.</p> <p>DMHC Response: The Office of Technology and Innovation and the HMO Help Center have implemented a "sleep to screensaver" solution to this issue. Once a clarify station has been idle for 15 minutes, the workstation will go to "sleep" and a screensaver will appear on the monitor. In order to reactivate the workstation the employee will need to input his user ID and password.</p> |
| <p><u>Finding 5</u> Incomplete and not timely recording of fixed assets into the inventory database system</p> | <p>SCO Reports: The department does not have procedures in place to properly record recently acquired assets into the Intellitrack system. The auditor tested fifteen assets that were recently acquired assets and concluded that five assets did not have acquisition dates and two items were not entered into Intellitrack. Not recording fixed assets into the inventory system once the assets are acquired will result in inaccurate accounting of State property. If the department does not enter an acquisition date into the system, it will be unable to identify assets recorded on the property ledger or to evaluate assets for possible disposition periodically.</p> <p>SCO Recommendation: The department should assign one person to update property ledgers with acquisition dates for assets over \$5,000 and record an acquisition date for each new entry to the property ledger once the asset is acquired. Reconciliation with the ledger can be simplified by using the date (fiscal month) on which the asset was recorded on the general ledger. However, any reasonable estimate of the acquisition date is preferable to a blank date field.</p> <p>DMHC Response: The Office of Technology and Innovation and the Business Management Unit recently revised their inventory control procedures, effective December 10, 2007. The new process now requires the Inventory Control Coordinator, in the Business Management Unit, to record all fixed assets. This includes IT and non-IT equipment. By following these new procedures, all assets will be recorded timely, into the Intellitrack System.</p> |